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Before the

FEDERAL COMMUNICATIONS COMMISSION

Washington, D.C. 20554

In the Matter of

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Federal-State Joint Board on

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Universal Service

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CC Docket No. 96-45

**FIFTH ORDER ON RECONSIDERATION and FOURTH REPORT AND ORDER  
IN CC DOCKET NO. 96-45**

Adopted: June 12, 1998

Released: June 22, 1998

By the Commission: Commissioners Ness and Tristani issuing separate statements;  
Commissioner Powell dissenting in part and issuing a separate statement; Commissioner  
Furchtgott-Roth dissenting and issuing a separate statement.

**TABLE OF CONTENTS**

	Par.
I. INTRODUCTION .....	1
II. ADJUSTMENT IN FUNDING YEAR FOR SCHOOLS AND LIBRARIES SUPPORT MECHANISM .....	6
III. COLLECTIONS DURING 1998 AND THE FIRST SIX MONTHS OF 1999 ...	15
IV. RULES OF PRIORITY FOR THE SCHOOLS AND LIBRARIES AND RURAL HEALTH CARE SUPPORT MECHANISMS .....	31
V. LEVEL OF COMPENSATION FOR OFFICERS AND EMPLOYEES OF THE ADMINISTRATIVE CORPORATIONS .....	43
VI. PUBLICATION OF QUARTERLY CONTRIBUTION FACTORS IN THE FEDERAL REGISTER .....	47

VII.	CONCLUSION .....	51
VIII.	SUPPLEMENTAL FINAL REGULATORY FLEXIBILITY ANALYSIS .....	54
IX.	ORDERING CLAUSES .....	67
APPENDIX A		
APPENDIX B		
APPENDIX C		
APPENDIX D		

## I. INTRODUCTION

1. In this Order, we reconsider, on our own motion, the Commission's decision regarding the funding year for the schools and libraries universal service support mechanism. We conclude that it is in the public interest to change the funding year for the schools and libraries universal service support mechanism from a calendar year cycle (January 1 - December 31) to a fiscal year cycle (July 1 - June 30). Moreover, we conclude that the transition to a fiscal year approach should be implemented immediately. Applications submitted during the initial 75-day filing window and approved for funding will, therefore, be funded through June 30, 1999, within the funding limitations adopted herein.

2. In this Order, we also reconsider, on our own motion, the Commission's decisions governing the amount of money that may be collected during the second six months of 1998 and the first six months of 1999 for the federal universal service support mechanisms for schools, libraries, and rural health care providers.<sup>1</sup> For the reasons set forth below, we find that we should modify the collection rate for the schools and libraries and rural health care support mechanisms for the third and fourth quarters of 1998 and the first and second quarters of 1999. We do not revise the annual caps adopted in the *Universal Service Order*.<sup>2</sup>

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<sup>1</sup> In light of pending petitions for reconsideration in this proceeding, the Commission retains jurisdiction to reconsider its own rules on its own motion. See 47 U.S.C. § 405, 47 C.F.R. § 1.108. See also *Central Florida Enterprises, Inc. v. FCC*, 598 F.2d 37, 48 n.51 (D.C. Cir. 1978), cert. dismissed, 441 U.S. 957 (1979).

<sup>2</sup> See Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report and Order*, 12 FCC Rcd 8776, 9002, 9054-62, 9139-45 (1997) (*Universal Service Order*), as corrected by Federal-State Joint Board on Universal Service, *Errata*, CC Docket No. 96-45, FCC 97-157 (rel. June 4, 1997), *appeal pending in Texas Office of Public Utility Counsel v. FCC and USA*, No. 97-60421 (5th Cir. 1997); Federal-State Joint Board on Universal Service, *Order on Reconsideration*, CC Docket No. 96-45, 12 FCC Rcd 10095 (rel. July 10, 1997); *Changes to the Board of Directors of the National Exchange Carrier Association Inc.*, Federal-State Joint Board on Universal Service, CC Docket Nos. 97-21, 96-45, *Report and Order and Second Order on Reconsideration*, 12 FCC Rcd 18400 (1997) (*NECA Report and Order*), as corrected by Federal-State Joint Board on Universal

Rather, we adjust the maximum amounts that may be collected and spent during 1998 and the first six months of 1999.

3. In this Order, we direct the Universal Service Administrative Company (USAC)<sup>3</sup> to collect only as much money as is required by demand, but in no event more than \$25 million per quarter for the third and fourth quarters of 1998 to support the rural health care universal service support mechanism, and no more than \$325 million per quarter for the third and fourth quarters of 1998 and the first and second quarters of 1999 to support the schools and libraries universal service support mechanism. Furthermore, we direct the administrative corporations (USAC, the Schools and Libraries Corporation, and the Rural Health Care Corporation) neither to commit nor disburse more than \$100 million during 1998 for the rural health care support mechanism, or more than \$1.925 billion for the schools and libraries support mechanism during 1998 and the first two quarters of 1999. Although these revised collection rates will not fully satisfy the estimated support requested by schools and libraries, we anticipate that the collection rates will ensure full support for telecommunications

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Service, *Errata*, CC Docket No. 96-45, DA 97-2477 (rel. Dec. 3, 1997); Changes to the Board of Directors of the National Exchange Carrier Association Inc., Federal-State Joint Board on Universal Service, CC Docket Nos. 97-21, 96-45, *Order on Reconsideration, Second Report and Order and Further Notice of Proposed Rulemaking*, 12 FCC Rcd 12444 (1997); Federal-State Joint Board on Universal Service, CC Docket Nos. 96-45, 97-160, *Third Report and Order*, 12 FCC Rcd 22485 (1997) (*Third Report and Order*), as corrected by Federal-State Joint Board on Universal Service, *Erratum*, CC Docket Nos. 96-45 and 97-160 (rel. Oct. 15, 1997); Changes to the Board of Directors of the National Exchange Carrier Association, Inc., Federal-State Joint Board on Universal Service, CC Docket No. 97-21, *Report and Order and Second Order on Reconsideration in CC Docket 97-21*, 12 FCC Rcd 22423 (1997); Federal-State Joint Board on Universal Service, CC Docket No. 96-24, *Third Order on Reconsideration*, 12 FCC Rcd 22801 (1997) (*Third Reconsideration Order*); Federal-State Joint Board on Universal Service, Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge, CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72, *Fourth Order on Reconsideration*, 13 FCC Rcd 5318 (1997) (*Fourth Reconsideration Order*), as corrected by Federal-State Joint Board on Universal Service, *Errata*, CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72, DA 98-158 (rel. Jan 29, 1998), appeal pending in *Alenco Communications, Inc., et al. v. FCC and USA*, No. 98-60213 (5th Cir. 1998).

<sup>3</sup> In the *NECA Report and Order*, the Commission established the administrative structure of the federal universal service support mechanisms, directing the National Exchange Carrier Association (NECA), as a condition of becoming temporary administrator of universal service, to create the Universal Service Administrative Company, the Rural Health Care Corporation, and the Schools and Libraries Corporation. *NECA Report and Order*, 12 FCC Rcd 18402. Among other functions, USAC collects funds from contributors and disburses those funds in accordance with the instructions of RHCC and SLC. 47 C.F.R. § 69.616. RHCC and SLC, in contrast, collect requests for support from applicants, commit funds to applicants, and monitor demand to ensure that the support mechanisms' annual monetary caps are not exceeded. 47 C.F.R. § 69.618-619. We have directed USAC, RHCC, and SLC to prepare and submit a joint plan of reorganization for approval by the Commission. See Report in Response to Senate Bill 1768 and Conference Report on H.R. 3579, *Report to Congress*, FCC 98-85 at 7, para. 10 (rel. May 8, 1998) (*May 8 Report*).

services and Internet access, and will also provide support for internal connections for the neediest applicants.

4. Consistent with this decision and in response to commenters' suggestions,<sup>4</sup> we also adopt new rules of priority for the schools and libraries mechanism to ensure further that schools and libraries with the greatest level of economic disadvantage will have priority for support and will receive the level of support established in the *Universal Service Order*.<sup>5</sup> In addition, we adopt a rule to pro-rate the distribution of support to health care providers if demand by health care providers exceeds the total fund allocated for a given funding year. Our decisions in this Order minimize burdens on subscribers, provide substantial support to schools, libraries, and health care providers, and enhance the Commission's previous efforts to ensure that the most disadvantaged schools and libraries receive funding priority.

5. In this Order, we also reconsider, consistent with the will of Congress, the level of compensation for the officers and employees of the Schools and Libraries Corporation (SLC) and the Rural Health Care Corporation (RHCC). We conclude that, as a condition of its continued service, the Administrator must compensate all officers and employees of the two independent corporations at an annual rate of pay, including any non-regular payments, bonuses, or other compensation, that does not exceed the rate of basic pay in effect for level I

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<sup>4</sup> See Great City Schools comments at 4 (proposing priority rules that would permit full funding for schools and libraries eligible for 80 percent and 90 percent discounts and a proportional scale back of discounts for all other eligible schools and libraries). See also Anchorage School Dist. Sept. 10 Public Notice comments at 1 (stating that, if sufficient funds are not available to meet all approved applications in subsequent filing periods, the Commission should apply an equal percentage reduction to all approved applicants during period); Mississippi Council for Ed. Tech. Sept. 10 Public Notice comments at 4 (asserting that funds should be available first to the most disadvantaged schools and libraries); Montana School Boards Ass'n Sept. 10 Public Notice comments at 3 (supporting a mechanism similar to the rules of priority should be applied to all funds, not just \$250 million); New York City Dept. of IT&T Sept. 10 Public Notice comments at 3 (stating that, if funds are exhausted within the window filing period, distribution of funds should be subject to a pro-rata reduction based on economic disadvantage, obviating need of a \$250 million trigger); New York Pub. Library Sept. 10 Public Notice comments at 1 (advocating a filing window and pro-rata allocation of funds when only \$500 million remains for the year). But see RUPRI comments at 3-4 (stating that sole reliance on poverty and urban/rural status is not the proper approach, but emphasis should be on total relative price after discount); Colorado Dept. of Ed. Sept. 10 Public Notice comments at 2 (opposing any proposal that limits the funds available to schools and libraries in the first six months because the Commission has chosen to collect only \$1 billion in the first six months); DataCast Sept. 10 Public Notice comments at 2 (favoring rules of priority that allocate 1/4 of all funds to rural, high cost schools and take into account "relative economic advantage" in allocating support); Illinois State Board of Dir. Sept. 10 Public Notice comments at 10-12 (favoring granting states greater authority in implementing rules of priority, favors granting priority to schools with the least amount of infrastructure, and favoring a higher trigger level because current 10 percent trigger represents insufficient funds); Maine Dept. of Ed. Sept. 10 Public Notice comments at 2 (favoring allocation of support according to the Technology Literacy Challenge Grants formula).

<sup>5</sup> See generally *Universal Service Order*, 12 FCC Rcd 8776 et seq..

of the Executive Schedule under section 5312 of Title 5 of the United States Code.<sup>6</sup> This rule will take effect on July 1, 1998. Finally, we reconsider, on our own motion, section 54.709 of the Commission's rules, which governs the date on which proposed universal service contribution factors become effective and eliminates the requirement that proposed contribution factors be published in the Federal Register. We conclude that, in the absence of further Commission action, the proposed contribution factors set forth in a Public Notice will be deemed approved 14 days after release of the Public Notice in which they are announced.

## II. ADJUSTMENT IN FUNDING YEAR FOR SCHOOLS AND LIBRARIES SUPPORT MECHANISM

### A. BACKGROUND

6. In the *Universal Service Order*, the Commission, among other things, established the federal universal service support mechanism for schools and libraries.<sup>7</sup> Consistent with the recommendations of the Federal-State Joint Board on Universal Service (Joint Board), the Commission concluded that all telecommunications services, Internet access, and internal connections would be provided at discounts ranging from 20 percent to 90 percent to eligible schools and libraries.<sup>8</sup> The Commission took these actions pursuant to and consistent with section 254 of the Communications Act, as amended by the Telecommunications Act of 1996,<sup>9</sup> and its accompanying legislative history.<sup>10</sup> For example, Congress explained that "[n]ew subsection (h) of Section 254 is intended to ensure that . . . elementary and secondary school *classrooms* and libraries have affordable *access* to modern telecommunications services."<sup>11</sup> Congress further stated that "[t]he ability of K-12 [kindergarten to 12th grade] *classrooms*, [and] libraries . . . to obtain *access* to advanced telecommunications services is critical to ensuring that these services are available on a universal basis."<sup>12</sup>

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<sup>6</sup> That pay rate is currently capped at \$151,800. See Exec. Order No. 13,071, 62 Fed. Reg. 68,521 (1997).

<sup>7</sup> *Universal Service Order*, 12 FCC Rcd at 9002-92.

<sup>8</sup> *Universal Service Order*, 12 FCC Rcd at 9002.

<sup>9</sup> Section 254 was added by the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996 Act), codified at 47 U.S.C. §§ 151 et seq. (Hereinafter, all citations to the 1996 Act will be to the 1996 Act as it is codified in the United States Code.) The 1996 Act amended the Communications Act of 1934 (the Act).

<sup>10</sup> See, e.g., S. Rep. No. 230, 104th Cong., 2d Sess. 131 (1996) (Joint Explanatory Statement).

<sup>11</sup> Joint Explanatory Statement at 132.

<sup>12</sup> Joint Explanatory Statement at 132-33 (emphasis added).

7. In the *Universal Service Order*, the Commission concluded that the funding year for schools and libraries would be the calendar year, and that applications for support would be accepted beginning on July 1 for the following year.<sup>13</sup> Schools and libraries are required to reapply for universal service support each year.<sup>14</sup> Moreover, for the first year of the support mechanism only, the Commission stated that requests for support would be accepted as soon as the schools and libraries website was opened and the applications were available.<sup>15</sup> In the *Third Report and Order*, the Commission adopted a filing window that would give equal funding priority to all schools, libraries, and health care providers filing during that window period and directed SLC and RHCC to determine the length of their filing windows.<sup>16</sup> Consistent with Commission direction, SLC adopted a filing window of 75 days,<sup>17</sup> which opened on January 30, 1998 and closed on April 15, 1998.<sup>18</sup>

## B. DISCUSSION

8. Upon reconsideration on our own motion, we find that it is in the public interest to change the funding year for the schools and libraries universal service support mechanism from a calendar year cycle (January 1 - December 31) to a fiscal year cycle that will run from July 1 - June 30. Moreover, we conclude that the transition to a fiscal year should be implemented immediately. In order to accommodate the transition to a fiscal year funding cycle, the first funding period will be the 18-month period that runs from January 1, 1998 through June 30, 1999. The second funding cycle, therefore, will begin on July 1, 1999. Applications submitted during the initial 75-day filing window and approved for funding by SLC, therefore, will be funded through June 30, 1999, to the extent permitted by funding constraints. Parties seeking support for the following fiscal year may begin to file applications on October 1, 1998. We direct SLC, in consultation with the Common Carrier Bureau, to establish a filing window for the next fiscal year, to open no later than October 1,

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<sup>13</sup> *Universal Service Order*, 12 FCC Rcd at 9057.

<sup>14</sup> *Universal Service Order*, 12 FCC Rcd at 9062.

<sup>15</sup> *Universal Service Order*, 12 FCC Rcd at 9057.

<sup>16</sup> *Third Report and Order*, 12 FCC Rcd at 22486.

<sup>17</sup> Schools and Libraries Corporation and Health Care Corporation Adopt Length of Filing Windows, *Public Notice*, CC Docket No. 96-45, DA 97-2349 (rel. Nov. 6, 1997) (*Windows Public Notice*).

<sup>18</sup> Also consistent with Commission direction to determine the length of its filing window, the Rural Health Care Corporation adopted a 75-day initial filing window. See *Windows Public Notice*. The rural health care filing window opened on May 1, 1998 and will close on July 14, 1998. We note that, consistent with the schools and libraries support mechanism, discounts on eligible services for eligible health care providers will be effective January 1, 1998 or the date services begin pursuant to the contract, whichever is later. See *infra* para. 9.

1998. We also conclude that SLC should determine the length of that window and resolve other administrative matters necessary to implement a filing window.<sup>19</sup>

9. We decide to implement a fiscal year funding cycle for schools and libraries, and to transition to this approach immediately, for several reasons. The immediate transition to a fiscal year approach will ameliorate the concerns of applicants seeking support for internal connections that they will be unable to complete installation before December 31, 1998, which marks the end of the funding year if determined on a calendar year basis.<sup>20</sup> We recognize that, because of the delay in issuing funding commitments to schools and libraries, many applicants may not be able to complete by this date the internal connections for which they have sought universal service support. The delay may be attributed to a variety of factors, including the Commission's decision to implement an initial filing window, and the Chairman's request to SLC to conduct an independent audit before disbursing any funds, in order to protect against waste, fraud, and abuse.<sup>21</sup> In short, the schools and libraries support mechanism is being implemented for the first time, and the Commission was not fully aware of the amount of time necessary to establish administrative systems that ensure program integrity and fair and orderly administration. Applicants could not have anticipated these delays at the time they conducted their technology needs assessments. Moreover, applicants understandably have been reluctant to begin service or initiate the installation of internal connections before receipt of a funding commitment. Nevertheless, schools and libraries that have worked diligently to comply with the Commission's requirements should not be burdened unnecessarily by this delay. To further accommodate schools and libraries affected by the delay in implementation, we note that discounts will be available on eligible services effective January 1, 1998 or the date services begin pursuant to the contract, whichever is later. Moreover, the transition to the fiscal year funding cycle adopted herein will afford applicants that will receive support for internal connections the flexibility to complete the installation of internal connections through June of 1999.<sup>22</sup>

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<sup>19</sup> This is consistent with previous directions to the administrative corporations. See *Third Report and Order*, 12 FCC Rcd at 22488.

<sup>20</sup> See *Santa Maria-Bonita School District, Request for Waiver* (dated Feb. 11, 1998) (*Santa Maria-Bonita Request for Waiver*).

<sup>21</sup> See, e.g., Letter from the Honorable William E. Kennard, Federal Communications Commission, to the Honorable John McCain, Chairman, Senate Committee on Commerce.

<sup>22</sup> *Santa Maria-Bonita Request for Waiver* at 1-2 (stating that, without an extension of time beyond December 31, 1998 to complete the installation of internal connections, "plans and specifications will have to be redrawn and rewritten . . . [t]he district would also need to cancel the current bid process and reissue bid documents starting a new bid cycle").

10. Furthermore, adopting a fiscal year funding cycle will synchronize the schools and libraries universal service support mechanism with the budgetary and planning cycles of most schools and libraries. This coordination of the support mechanism with the applicants' internal administrative processes will enable schools and libraries to plan their technology needs in a more efficient and organized manner. In addition, using a fiscal year funding cycle will align universal service contribution levels with the local exchange carrier annual access tariff filing schedule. Under our rules, local exchange carriers file their annual tariffs to be effective July 1 of each year.<sup>23</sup> One piece of information these companies require in order to file their tariffs is the universal service contribution factors.

11. We recognize that, under the approach adopted herein, some schools and libraries that did not file within the initial window in 1998 will not be eligible to receive funding until July 1999, rather than January 1999. We find, however, that on balance, the benefits that will be conferred on the approximately 30,000 applicants that filed within the initial window outweigh the hardship caused by the potential six-month delay in funding for some applicants. We also find that this approach strikes the best balance between fulfilling the statutory mandate to enhance access to advanced telecommunications and information services for schools and libraries, and fulfilling the statutory principle that "[q]uality services should be available at just, reasonable, and affordable rates."<sup>24</sup>

12. To accomplish this change, we conclude that the following revisions in the funding cycle must be implemented. First, for applications filed within the initial 75-day filing window seeking discounts on telecommunications services and Internet access, the Administrator shall make funding commitments effective for services provided no earlier than January 1, 1998. These services will be funded at the approved monthly level, consistent with the information included on the school's or library's application, through June 30, 1999. We conclude that this approach is reasonable because telecommunications services and Internet access are generally provided at regular, monthly intervals and are billed on a monthly, recurring basis.

13. Second, for applications filed within the initial 75-day filing window seeking discounts on internal connections, the Administrator shall commit the approved amount of support, but these funds may be utilized during the remainder of 1998 as well as during the transition period through June 30, 1999. We conclude that this approach is reasonable because, unlike telecommunications services and Internet access, internal connections generally entail nonrecurring rather than recurring costs.<sup>25</sup> Moreover, installation of internal

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<sup>23</sup> See 47 C.F.R. § 69.3(a).

<sup>24</sup> 47 U.S.C. § 254(b)(1).

<sup>25</sup> See McKinsey and Company, *Connecting K-12 Schools to the Information Superhighway* at Appendix A.



connections frequently requires that the projects be timed to occur during periods when school is out of session and students are not present in instructional buildings. Thus, the installation of internal wiring might be completed in stages during winter and summer vacation periods. Accordingly, we amend section 54.507(b) of our rules, as provided in Appendix A.

14. The transition to a fiscal year funding cycle adopted herein requires that we reconsider on our own motion the limitation on the exemption from competitive bidding for voluntary extensions of contracts. Our rules currently provide that voluntary extensions of existing contracts are not exempt from the competitive bidding rules.<sup>26</sup> In order to accomplish an orderly transition to the fiscal year funding cycle, however, we conclude that we must allow existing contracts that have a termination date between December 31, 1998 and June 30, 1999 to be voluntarily extended to a date no later than June 30, 1999. Although voluntary extensions of contracts generally are not exempt from the competitive bidding requirement,<sup>27</sup> we adopt this limited exception for voluntary extensions of contracts up to June 30, 1999. To hold otherwise would result in schools and libraries either having to participate in competitive bidding for only a six month service period or not being eligible for support for that six month period. We conclude that either result would be both administratively and financially unworkable for schools and libraries. We find, therefore, that it is in the public interest to amend the exemption (in section 54.511 of our rules) from the competitive bidding requirements, to allow schools and libraries that filed applications within the 75-day initial filing window to extend voluntarily, to a date no later than June 30, 1999, existing contracts that otherwise would terminate between December 31, 1998 and June 30, 1999.

### III. COLLECTIONS DURING 1998 AND THE FIRST SIX MONTHS OF 1999

#### A. BACKGROUND

15. Because these newly-created support mechanisms had no historical data of their own upon which to estimate with certainty the demand for services in the initial months of the support mechanisms,<sup>28</sup> the Federal-State Joint Board on Universal Service and the Commission relied on the figures submitted on the record in the Universal Service proceeding to project demand for the schools and libraries and rural health care universal service support

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<sup>26</sup> See 47 C.F.R. § 54.511(d); see also 47 C.F.R. § 54.504. Our rules state that the following contracts are exempt from our competitive bidding requirements: contracts signed on or before July 10, 1997 are exempt for the life of the contract; and contracts signed after July 10, 1997 but before January 30, 1998 are exempt only with respect to services provided between January 1, 1998 and December 31, 1998. 47 C.F.R. § 54.511(c)(1).

<sup>27</sup> See *Universal Service Order*, 12 FCC Rcd at 9062-63, para. 545.

<sup>28</sup> *Universal Service Order*, 12 FCC Rcd at 9054-56, 9140-41.

mechanisms.<sup>29</sup> Based on extensive public comment and the unanimous recommendation of the bipartisan Joint Board,<sup>30</sup> the Commission instituted annual caps on both support mechanisms -- \$2.25 billion for the schools and libraries support mechanism,<sup>31</sup> and \$400 million for the rural health care support mechanism.<sup>32</sup> In addition, the Commission specified that the Administrator should collect \$100 million per month for the first three months of 1998 for the schools and libraries support mechanism,<sup>33</sup> and held that, between January 1, 1998 and June 30, 1998, the Administrator "will only collect as much as required by demand, but in no case more than \$1 billion."<sup>34</sup> For the rural health care support mechanism, the Commission directed the Administrator to collect \$100 million for the first three months of 1998.<sup>35</sup> On December 16, 1997, the Commission adopted the *Third Reconsideration Order*. The *Third Reconsideration Order* revised the collection amounts, directing the administrator to collect and spend no more than \$50 million for the first six months of 1998 to support the rural health care universal service support mechanism and no more than \$625 million for the first six months of 1998 to support the schools and libraries universal service support mechanism.<sup>36</sup> The Commission took this action because it did not want to impose unnecessary financial requirements on service provider contributors to universal service by requiring the collection of funds that were not needed to meet demand for universal service assistance.<sup>37</sup>

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<sup>29</sup> See Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Recommended Decision*, 12 FCC Rcd 87, 368-71 (1996); *Universal Service Order*, 12 FCC Rcd at 9054-57.

<sup>30</sup> See *Recommended Decision*, 12 FCC Rcd at 368-71.

<sup>31</sup> *Universal Service Order*, 12 FCC Rcd at 9054.

<sup>32</sup> *Universal Service Order*, 12 FCC Rcd at 9141.

<sup>33</sup> *Universal Service Order*, 12 FCC Rcd at 9056.

<sup>34</sup> *Universal Service Order*, 12 FCC Rcd at 9054. The Commission further directed the administrator to "adjust future contribution assessments quarterly based on its evaluation of schools and library demand for funds, within the limits of the spending caps . . . ." *Id.* at 9055-56.

<sup>35</sup> *Universal Service Order*, 12 FCC Rcd at 9145.

<sup>36</sup> *Third Order on Reconsideration*, 12 FCC Rcd 22801 (1997).

<sup>37</sup> *Third Reconsideration Order*, 12 FCC Rcd at 22803-04. Based on what it learned about the status of preparatory arrangements being made by schools and libraries to obtain the benefit of the universal service support mechanism, the Commission concluded that demand for the schools and libraries support mechanism would not exceed \$625 million in the first and second quarters of 1998. *Id.*

16. When it adopted the annual funding caps in the *Universal Service Order* in May 1997, the Commission anticipated that funds would begin to flow on January 1, 1998.<sup>38</sup> In making that estimate, the Commission did not take fully into account the amount of time necessary for the administrative corporations to establish administrative systems that not only will provide the highest level of service to eligible schools, libraries, and health care providers, but that will ensure that federal universal service funds are not subject to waste, fraud, and abuse. Due to those efforts to maximize the adequacy, efficiency, and accountability of the support mechanisms, and due to the filing window that the Commission adopted to ensure equitable treatment of schools, libraries, and health care providers, eligible entities could not begin to receive commitments for funding until after mid-April 1998, when the initial filing window closed.<sup>39</sup> Funds for the schools and libraries support mechanism will not begin to be disbursed until July 1998, at the earliest, and funds for the rural health care support mechanism likely will not begin to be disbursed before the third quarter of 1998.

17. As of May 1, 1998, SLC estimated that \$2.02 billion in discounts had been requested by applicants that had filed for schools and libraries discounts through April 28, 1998.<sup>40</sup> RHCC projected that the rural health care support mechanism will require \$25 million for the third quarter.<sup>41</sup> On May 13, 1998, the Common Carrier Bureau released a Public Notice seeking comment on a proposed revision of the 1998 collection amounts for the schools and libraries and rural health care universal service support mechanisms.<sup>42</sup> In the *Collection Public Notice*, the Common Carrier Bureau sought comment on a proposal to direct USAC to collect only as much money as is required by demand, but in no event more than \$25 million per quarter for the third and fourth quarters of 1998 to support the rural health care universal service support mechanism, and no more than \$524 million per quarter for the

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<sup>38</sup> *Universal Service Order*, 12 FCC Rcd at 9092.

<sup>39</sup> In the *Third Report and Order*, the Commission adopted a filing window that will give equal funding priority to all schools, libraries, and health care providers that file during that window period. *Third Report and Order*, 12 FCC Rcd 22485. Consistent with Commission direction to determine the length of the filing windows, SLC and RHCC adopted windows of 75 days. Schools and Libraries Corporation and Health Care Corporation Adopt Length of Filing Windows, CC Docket No. 96-45, *Public Notice*, DA 97-2349 (rel. Nov. 6, 1997). The schools and libraries filing window opened on January 30, 1998 and closed on April 15, 1998. The rural health care filing window opened on May 1, 1998 and will close on July 14, 1998.

<sup>40</sup> Third Quarter 1998 Fund Size Requirements for the Schools and Libraries Universal Service Program, dated May 1, 1998, at 2 (filed by SLC).

<sup>41</sup> Third Quarter 1998 Projected Demand and Expenses for the Rural Health Care Universal Service Support Program, dated May 1, 1998, at 1 (filed by RHCC).

<sup>42</sup> Common Carrier Bureau Seeks Comment on Proposed Revision of 1998 Collection Amounts for Schools and Libraries and Rural Health Care Universal Service Support Mechanisms, *Public Notice*, CC Docket No. 96-45, DA 98-872 (rel. May 13, 1998) (*Collection Public Notice*).

third and fourth quarters of 1998 to support the schools and libraries universal service support mechanism. The Common Carrier Bureau also sought comment on whether to direct the administrative corporations neither to commit nor disburse more than \$100 million for the health care support mechanism and \$1.67 billion for the schools and libraries support mechanism during the 1998 funding year.<sup>43</sup>

## B. DISCUSSION

18. Consistent with section 254 of the Act, and the recommendations of the Federal-State Joint Board on Universal Service,<sup>44</sup> we remain committed to providing support to eligible schools and libraries for telecommunications services, Internet access, and internal connections.<sup>45</sup> We share the concerns of commenters that curtailing collections may have adverse impacts on schools and libraries, particularly the neediest of those entities.<sup>46</sup> We, therefore, remain dedicated to providing support in a manner that targets the most economically disadvantaged schools and libraries. At the same time, we are cognizant of the concerns of many legislators that we must balance the need to provide support for schools and libraries against the need to continue to provide support for high cost carriers, and to keep

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<sup>43</sup> *Collection Public Notice* at 4.

<sup>44</sup> *See Recommended Decision*, 12 FCC Rcd 87.

<sup>45</sup> We note that Secretary Riley of the United States Department of Education (Department of Education) recently responded to a General Accounting Office (GAO) report that identified 40 programs in nine federal agencies, funded at more than \$10 billion, that support the acquisition of telecommunications technologies for schools and libraries. *See* Letter from Secretary Richard W. Riley, United States Department of Education to James F. Hinchman, Acting Comptroller General, GAO, dated June 8, 1998 (citing GAO, Telecommunications: Court Challenges to FCC's Universal Service Order and Federal Support for Telecommunications for Schools and Libraries (rel. May 7, 1998)). Secretary Riley characterized the GAO report as "very misleading," stating that "[o]f the \$8.2 billion identified from Department of Education programs, we estimate that only about \$590 million is available specifically for education technology-related programs, and that only a very small percentage of that amount is used to support telecommunications." *Id.* at 1. Secretary Riley also noted that "[t]he Technology Literacy Challenge Fund and other, smaller sources of Federal funding for technology would work in conjunction with the E-Rate discounts to help schools use the Internet effectively, but by no means could they take the place of the E-Rate in providing and maintaining Internet access." *Id.* at 2.

<sup>46</sup> *See, e.g.,* Letter from the Honorable Ted Kennedy, the Honorable Jay Rockefeller, the Honorable Bob Kerrey, the Honorable Chris Dodd, the Honorable Jim Jeffords, the Honorable Rick Santorum, the Honorable John Chafee, and the Honorable Olympia Snowe, dated May 22, 1998, at 1 (stating that "modern technology can level the playing field"); NTIA comments at 2 (stating that "[n]o school or child must be excluded from the benefits of the information age because of income or geographical area"); Letter from the Honorable Jay Rockefeller, the Honorable Bob Kerrey, and 32 Senators, United States Senate, dated June 10, 1998, at 1 (stating that "[u]niversal means just that -- urban, suburban and rural; poor and rich; public and private; all races and ethnic groups . . . [n]o child or family should be left behind").

telephone rates affordable throughout the country.<sup>47</sup> We note that, pursuant to the 1996 Act, the Commission has taken significant action to implement the universal service provisions of the Act. At the present time, the rural, insular, and high cost telephone subscribers continue to receive high cost support at the same level that they have received for years. In addition, one of the first steps in universal service reform was to make existing high cost support explicit.<sup>48</sup> Moreover, we have expanded the Commission's low-income programs, Lifeline Assistance (Lifeline) and Lifeline Connection Assistance (Link Up).<sup>49</sup> For example, we adopted the Joint Board's recommendation that Lifeline service should be provided to low-income consumers nationwide, even in states that had not previously participated in Lifeline, and that all eligible telecommunications carriers should be required to provide Lifeline service.<sup>50</sup> The Commission remains committed, pursuant to section 254, to implementing all parts of universal service.

19. We find, therefore, that it is prudent to begin funding collections for a new mechanism at a reduced level, and allow for the possibility of increased collections in the future. We note that this phase-in approach to funding is consistent with the decision in the *Universal Service Order*, and with the initial funding for high cost support when NECA began its high cost collection and distribution efforts in 1986.<sup>51</sup> In providing support for schools, libraries, and rural health care providers, we strive to ensure a smooth transition to the new universal service support mechanisms and to minimize disruption to consumers. We find that our decision to adjust the maximum amounts that may be collected or spent in 1998 is consistent with these goals.

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<sup>47</sup> See Letter from the Honorable Tom Bliley, Chairman, House Committee on Commerce, the Honorable John D. Dingell, Ranking Minority Member, House Committee on Commerce, the Honorable John McCain, Chairman, Senate Committee on Commerce, and the Honorable Ernest F. Hollings, Ranking Minority Member, Senate Committee on Commerce, to the Honorable William E. Kennard, Chairman, Federal Communications Commission, dated June 4, 1998; Letter from the Honorable John D. Dingell, Ranking Minority Member, House Committee on Commerce, to the Honorable William E. Kennard, Chairman, Federal Communications Commission, dated June 4, 1998.

<sup>48</sup> See, e.g., *Universal Service Order*, 12 FCC Rcd at 9165 (removing Long Term Support (LTS) from access charges); 12 FCC Rcd at 8940-41 (stating that "[w]e adopt the Joint Board's recommendation that a subsidy corresponding in amount to that generated formerly by DEM [dial equipment minutes] weighting be recovered from the new universal service support mechanisms").

<sup>49</sup> See generally *Universal Service Order*, 12 FCC Rcd at 8952-94.

<sup>50</sup> *Universal Service Order*, 12 FCC Rcd at 8952. In late February 1998, eligible telecommunications carriers began submitting to USAC requests for reimbursement for offering Lifeline service to low-income consumers. Federal Universal Service Programs Fund Size Projections & Contribution Base for Third Quarter 1998, filed by USAC, dated May 1, 1998, at 12.

<sup>51</sup> See 47 C.F.R. §§ 36.631 and 36.64.

20. We therefore find that we should not increase the quarterly collection amounts at this time with respect to the schools and libraries and rural health care support mechanisms. We therefore conclude that establishing quarterly collection rates for the schools and libraries support mechanism of \$325 million for each of the third and fourth quarters of 1998 and the first and second quarters of 1999 will preserve the dual statutory mandates to maintain affordable rates throughout the country and to "enhance . . . access to advanced telecommunications and information services for all public and non-profit elementary and secondary school classrooms . . . and libraries."<sup>52</sup> These collection rates maintain current collection rate levels and will not increase interstate telecommunications carriers' costs of providing service. Moreover, these collection rate levels should ensure that long distance rates, overall, will continue to decline.<sup>53</sup> At the same time, based on the estimated demand for support by schools and libraries that filed applications during the initial 75-day filing window, these collection rates will be sufficient to fully fund requests for support for telecommunications services, and Internet access, and to fully fund requests by the neediest schools and libraries for support for internal connections. The remaining requests for support for internal connections would be funded in the manner set forth in Section III, herein.

21. We further conclude that we should establish maximum collection rates for the rural health care support mechanism at \$25 million for each of the third and fourth quarters of 1998. These collection rates are consistent with projected demand and there is no evidence that eligible health care providers will require additional funding this year. Consistent with the *Universal Service Order*, we do not want USAC to collect funds that exceed demand.<sup>54</sup> Because the rural health care support mechanism will continue to be funded on a calendar, rather than a fiscal, year basis, and because the mechanism is still in the very early stages, we find that we should not adopt maximum collection rates beyond 1998. Instead, we will evaluate the 1999 collection rates for the rural health care support mechanism in the future.

22. The universal service support mechanisms will provide substantial support to schools, libraries, and health care providers without imposing unnecessary burdens on

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<sup>52</sup> 47 U.S.C. § 254(h)(2).

<sup>53</sup> On June 16, 1998, incumbent local exchange carriers will file new access tariffs with rates to become effective on July 1, 1998. Based on preliminary information filed by these carriers on April 2, 1998, we estimate their total access charge revenues to decline by approximately \$720 million below current levels, measured on an annualized basis at current demand levels. The *Third Quarter Contribution Factors Public Notice*, released by the Common Carrier Bureau upon adoption of this Order, will produce a reduction in total interexchange carrier payments of approximately \$85 million. See Third Quarter 1998 Universal Service Contribution Factors Revised and Approved, CC Docket No. 96-45, *Public Notice*, DA 98-1130 (rel. June 12, 1998). Based on this, total interexchange carrier payments for access services and universal service contributions should decrease by approximately \$800 million on July 1, 1998.

<sup>54</sup> See *Universal Service Order*, 12 FCC Rcd at 9145 (stating that collection for the rural health care universal service support mechanism would be based on demand).

consumers, and the most economically disadvantaged schools and libraries will receive the greatest share of support, consistent with the discount matrix contained in the *Universal Service Order*.<sup>55</sup> We seek to provide support to schools, libraries, and rural health care providers in a manner that does not require consumers' rates to rise and without causing rate churn. Some commenters assert that a certain amount of rate churn is to be expected in a competitive marketplace.<sup>56</sup> That may be true, but we remain committed to ensuring that universal service does not exacerbate any rate churn that may already exist in the marketplace. Excessive and unnecessary rate churn would be disruptive to consumers, a result we wish to avoid.

23. Numerous commenters take issue with the Commission's proposal to revise collections for the schools and libraries and rural health care universal service support mechanisms consistent with anticipated reductions in access charges.<sup>57</sup> We agree with the Alaska Commission that funding for the new universal service support mechanisms "must be balanced against potential impact on rates and universal service,"<sup>58</sup> and that is precisely the approach we are adopting. We conclude, therefore, that a gradual phase-in of the schools, libraries, and rural health care universal service support mechanisms that takes advantage, and reflects the timing, of access charge reductions will provide substantial support for eligible services ordered by eligible schools, libraries and rural health care providers, and at the same time will avoid disruption to consumers.

24. Many commenters note that schools and libraries have expended substantial resources, in terms of both time and money, in applying for discounted services, all with the

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<sup>55</sup> *Universal Service Order*, 12 FCC Rcd at 9050.

<sup>56</sup> See, e.g., AirTouch comments at 5 n.10 (stating that changing rates are to be expected in a competitive marketplace); Nassau BOCES comments at 3-4 (asserting that rate churn is a fact of life under competitive conditions).

<sup>57</sup> See, e.g., Bell Atlantic comments at 3-4 (asserting that, because access charges are dictated by a price cap formula, the Commission cannot impose additional reductions in access charges to fund universal service); EdLiNC comments at 1-3 (stating that linking access charge reductions to universal service funding is inconsistent with section 254's mandate to establish a discount mechanism adequate to meet the congressional goal of providing all schools and libraries will affordable access to advanced telecommunications and information services); NC DPI comments at 4 (stating that the law does not require that access charges and universal service funding be linked and that the Commission should not act to make that happen); Time Warner comments at 3-4 (asserting that the Commission should establish a universal service fund that is sufficient to address the policy goals of affordability for basic telecommunications services and support of eligible services for schools, libraries, and rural health care provider but that is not tied to access charge reductions).

<sup>58</sup> Alaska Commission comments at 4.

expectation that a maximum of \$2.25 billion in funding would be available.<sup>59</sup> We share the concern of the U.S. Department of Education and other commenters that schools and libraries require predictability of funding to facilitate long-range technology planning, and that our actions here should not discourage schools and libraries from seeking universal service support.<sup>60</sup> We agree that the submission of over 30,000 applications demonstrates substantial demand for universal service support for schools and libraries,<sup>61</sup> and we applaud the entities that have worked diligently to comply with our rules. We are troubled by the disruption imposed on schools and libraries and we hope to avoid this situation in the future. At the same time, we must be mindful of the effects of the schools and libraries and rural health care support mechanisms on consumers. If we were to fund these support mechanisms to the full amount of the caps adopted in the *Universal Service Order*, there would be negative

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<sup>59</sup> See, e.g., Funds for Learning comments at 2 (stating that schools and libraries have spent time completing applications and designing technology plans and have modified or delayed installation schedules, all in reliance on the availability of \$2.25 billion); NC Governor comments at 1-2 (supporting full funding because of tremendous effort, especially in terms of human resources, to participate in universal service); EdLiNC comments at 3-5 (stating that schools and libraries have devoted substantial resources, made contractual commitments, and issued bonds with the expectation that universal service would be funded up to the amount recommended by the Joint Board and adopted a year ago by the Commission); Great City Schools comments at 3 (stating that the submission of over 30,000 applications is evidence that schools and libraries have relied upon the expectation of full funding and have had to devote substantial resources toward applying for universal service discounts).

<sup>60</sup> See U.S. Department of Education comments at 1. See also Letter from Richard W. Riley, Secretary of Education, William M. Daley, Secretary of Commerce, Daniel R. Glickman, Secretary of Agriculture, and Donna E. Shalala, Secretary of Health and Human Services to William E. Kennard, Chairman of the Federal Communications Commission, dated June 8, 1998 (stating that the Commission should "strongly support the e-rate" because "delaying or undermining its effectiveness will heighten the risk of economic inequality and social division"); DTG comments at 4-5 (stating that "[t]he proposed revision of support collections after the initial round of applications is final imposes new risk and unpredictability on the process at a time when it should become more predictable if the goal of access to advanced telecommunications for all schools is to be met"); NC DPI comments at 3 (changing the rules at this point causes mistrust and economic hardship); Funds for Learning comments at 2 (asserting that schools and libraries need predictability, not more frustration, and that service providers may become disenchanted with the changing rules and potential loss of business as schools and libraries have to delay projects for which they anticipated receiving support). We note here that the Santa Maria-Bonita School District proposed an alternative to the proposed collection amounts described in the *Collection Public Notice*, under which an additional \$350 million would be collected in 1998, followed by a \$350 million reduction in collections in 1999. See Santa Maria-Bonita School District comments at 2-3. Because this proposal would not mitigate the problem of rate churn that it would impose upon consumers, we must reject it.

<sup>61</sup> See, e.g., Letter from the Honorable Ted Kennedy, the Honorable Jay Rockefeller, the Honorable Bob Kerrey, the Honorable Chris Dodd, the Honorable Jim Jeffords, the Honorable Rick Santorum, the Honorable John Chafee, and the Honorable Olympia Snowe, United States Senate, dated May 22, 1998 (stating that the number of applications submitted demonstrates the "importance of the program and the nationwide need for this financial assistance"). New Jersey Library Association comments at 2 (stating that initial response demonstrates the need for the schools and libraries support mechanism); EdLiNC comments at 4 (stating that the submission of over 30,000 applications validates the need for and the importance of universal service for schools and libraries).



consequences for consumers. Congress mandated that universal service has many components, including support for schools, libraries, and rural health care providers, as well as the directive to maintain rates at an affordable level.<sup>62</sup> We conclude, therefore, that reducing the collection rates for the schools and libraries and rural health care support mechanisms during the initial implementation is consistent with the Act and is the most prudent course to take at this time.

25. Several commenters maintain that revising collections levels for the schools and libraries and rural health care support mechanisms to match projected reductions in access charges would impose an unreasonable and disproportionate burden on CMRS and other wireless providers that do not pay access charges,<sup>63</sup> and that such an approach would not be competitively neutral.<sup>64</sup> One of the dissenting statements similarly suggests that wireless carriers are being disproportionately burdened because they do not pay access charges.<sup>65</sup> We note first that we are not here adopting our proposal in the *Collection Public Notice* to increase schools and libraries funding to levels that match projected reductions in access charges paid by long-distance carriers. We are instead freezing for the next four quarters the contribution levels in place during the second quarter of 1998. Thus, no carrier will experience increased universal service obligations as a result of an increase in funding for the schools and libraries support mechanism. Second, we find that CMRS and other wireless carriers are not disproportionately burdened because they pay universal service obligations even though they do not benefit from access charge reductions. Before passage of the 1996 Act, only interstate long-distance carriers paid for universal service in the interstate jurisdiction, either directly or through access charges. The 1996 Act, however changed that by requiring universal service to be supported by all interstate telecommunications carriers, whether or not they had previously paid access charges. The point of the 1996 Act in this respect was to end the existing discriminatory treatment of long-distance carriers, and impose

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<sup>62</sup> 47 U.S.C. § 254(b)(1) (stating that "[q]uality services should be available at just, reasonable, and affordable rates").

<sup>63</sup> See, e.g., AirTouch comments at 2 (stating that the proposed revision in collection amounts would "unlawfully discriminate against wireless carriers and others who do not accrue any benefits from access charge reductions"); CTIA comments at 4-5 (asserting that the proposed revision imposes an unreasonable burden on CMRS and other providers that do not pay access charges); PCIA comments at 2-3 (stating that the proposed revision will disproportionately impact CMRS providers); MACTel comments at 2-3 (stating that the proposed revision will disproportionately increase the universal service burden on CMRS providers and will reduce CMRS penetration rates in rural and insular areas because the cost of CMRS service will increase).

<sup>64</sup> GTE comments at 7 (stating that the proposed revision in collection amounts would not be competitively neutral because wireless and paging carriers that do not pay access charges will not enjoy the benefits of reduced access charges and will, therefore, have to increase their charges to offset increased universal service contribution obligations).

<sup>65</sup> Statement of Commissioner Harold Furchtgott-Roth, dated June 22, 1998, at 4.

universal service obligations as well on other interstate carriers, including CMRS carriers. The 1996 Act also established that universal service be funded in a competitively neutral manner. To implement that, we have required that all interstate telecommunications carriers contribute to universal service based on end-user revenues.<sup>66</sup> We continue to believe that to be a reasonable approach to implementing the competitive neutrality requirements of the Act. Finally, to the extent that the *Collection Public Notice* noted the relation between universal service obligations and access charge reductions, it was simply to note that overall the Commission's actions have reduced the cost of providing long distance service -- an issue of significant public interest. We note similarly here that, since passage of the 1996 Act, competition and changes in reciprocal compensation arrangements between CMRS providers and local exchange carriers (LECs) have helped provide for the lowest wireless prices for consumers in history, despite wireless carriers' contributions to universal service.

26. The contention in one of the dissents that universal service contributions, at least to the extent used to provide support for non-telecommunications services, constitute an unlawful tax is neither new nor correct.<sup>67</sup> As the Commission has found previously, contributions to the universal service mechanisms do not represent taxes enacted under Congress's taxing authority. Rather, they constitute fees enacted pursuant to Congress's Commerce power. We noted previously that the contribution requirements do not violate the Origination Clause of the Constitution because "universal service contributions are not commingled with government revenues raised through taxes,"<sup>68</sup> and universal service support mechanisms therefore are not a "general welfare scheme" of the type found by courts to be taxes.<sup>69</sup> In *United States v. Munoz-Flores* and elsewhere, the Supreme Court has held that Congress does not exercise its taxing powers when funds are raised for a specific government program. Universal service contributions are deposited into a specific fund established as part of the universal service mechanisms to provide money support for those mechanisms and therefore do not constitute taxes.

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<sup>66</sup> See *Universal Service Order*, 12 FCC Rcd at 9206.

<sup>67</sup> Statement of Commissioner Harold Furchtgott-Roth, dated June 22, 1998, at 13-16.

<sup>68</sup> *Fourth Reconsideration Order*, 13 FCC Rcd at 5465.

<sup>69</sup> *Universal Service Order*, 12 FCC Rcd at 9188-89. See *United States v. Munoz-Flores*, 495 U.S. 385, 398 (1990) ("special assessment" on any person convicted of a federal misdemeanor to be deposited into a Crime Victim's Fund was not a tax); see also *Response of Federal Communications Commission to Motion for Stay of Celpage, Inc., Texas Office of Public Utility Counsel v. FCC and USA, No 97-60241 (5th Cir.) (Texas Public Utility Counsel Stay Opposition)* at 14-17, and cases cited therein. On delegation issues, see, e.g., *Universal Service Order*, 12 FCC Rcd at 9003-23, 9084-90, 9203-05; Brief for Federal Communications Commission in *Texas Public Utility Counsel (Texas Public Utility Counsel Brief)* at 165-172, 173-177, 183-188.

27. Our conclusion that universal service contributions are not a tax is not changed by the citation to *Thomas v. Network Solutions, Inc.*<sup>70</sup> There, the court found that part of the charge made by the National Science Foundation's contractor for the registration of internet domain names was a tax rather than a fee because it provided "revenue for the government for projects that did not directly benefit the payees or otherwise apply to the purposes furthered by the [agreement between the NSF and its contractor]." <sup>71</sup> Here, by contrast, universal service contributions are not intended to raise general revenue as they are placed in a segregated fund dedicated for a specific regulatory purpose, and, as we have noted previously, all telecommunications carriers required to contribute benefit from the ubiquitous telecommunications network that universal service makes possible.<sup>72</sup> Even if this were not the case, *Munoz-Flores* rejects the proposition that a charge is a tax unless the payees benefit from its payment.<sup>73</sup>

28. Finally, we note that the argument that universal service contributions for the schools and libraries mechanisms constitutes an unlawful tax can be and has been made with respect to the entire universal service program.<sup>74</sup> This argument proves too much. If that interpretation were correct, the entire universal service program, including support for service to rural and high cost areas, would constitute an unlawful tax. This interpretation is incorrect because, as noted above, Congress need not exercise its taxing powers to fund a specific government program through fees. This is precisely what Congress has done with respect to universal service.

29. We find, therefore, that it serves the public interest to adjust the amounts that the Commission directed the Administrator to collect and spend for the second six months of 1998, as described herein. We amend our previous decision, and direct USAC to collect only as much as required by demand, but in no event more than \$25 million per quarter for the third and fourth quarters of 1998 for the rural health care universal service support mechanism. We direct USAC to collect only as much as required by demand, but in no event more than \$325 million per quarter for the third and fourth quarters of 1998 and the first and second quarters of 1999 to support the schools and libraries universal service support mechanism. We also direct RHCC to commit to applicants no more than \$100 million for

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<sup>70</sup> 1998 WL 191205 (D.D.C.).

<sup>71</sup> *Id.*

<sup>72</sup> *Universal Service Order*, 12 FCC Rcd at 9188-89.

<sup>73</sup> 495 U.S. at 400; see also cases cited in *Texas Public Utility Counsel Stay Opposition* at 13-16; *Head Money Cases (Edye v. Robertson)*, 112 U.S. 580 (1884).

<sup>74</sup> See Brief of Celpage, *Texas Office of Public Utility Counsel v. FCC and USA*, No. 97-60421 (5th Cir. 1997) (appeal pending).

disbursement during 1998, and direct SLC to commit to applicants no more than \$1.925 billion for disbursement during 1998 and the first half of 1999. The adoption of these limits on disbursements supersedes any prior restrictions on expenditures during 1998.<sup>75</sup>

30. Furthermore, we conclude that the carryover of unused funding authority will not apply for the funding period January 1, 1998 through June 30, 1999. That is, to the extent that the amounts collected in the funding period January 1, 1998 through June 30, 1999 are less than \$2.25 billion, the difference will not be carried over to subsequent funding years. Consistent with the phased-in approach to funding for the schools and libraries and rural health care support mechanisms that we have adopted herein, we find it unnecessary to carry over unused funding authority. To the extent that funds are collected but not disbursed in the funding period January 1, 1998 through June 30, 1999, however, those collected funds would be carried over to the next funding period. Accordingly, we amend section 54.507(a) and section 54.623(a) of our rules, as provided in Appendix A.

#### **IV. RULES OF PRIORITY FOR THE SCHOOLS AND LIBRARIES AND RURAL HEALTH CARE SUPPORT MECHANISMS**

##### **A. BACKGROUND**

31. In the *Universal Service Order*, the Commission initially concluded that schools and libraries would receive universal service discounts on a first-come, first-served basis.<sup>76</sup> Discounts for schools and libraries are allocated according to a discount matrix which assigns discount levels to schools and libraries based on whether a school or library is located in a rural area and on the percentage of students who are eligible for the national school lunch program in a given school or school district.<sup>77</sup> For example, schools in which at least 75 percent of the students are eligible for the school lunch program receive a 90 percent discount on rates for telecommunications services, Internet access, and internal connections. The discount rate falls as low as 20 percent in the case of an urban school with fewer than 1 percent of its students eligible for the lunch program. To protect the most disadvantaged schools and libraries, the Commission adopted rules of priority that go into effect when only \$250 million remains available for allocation toward school and library discounts.<sup>78</sup> As adopted, the rules of priority require SLC to allocate remaining funds to provide discounts to

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<sup>75</sup> Prior to adoption of this Order, sections 54.507(a) and 54.623(a) of our rules provided that no more than a specified monetary amount could be collected or spent during the first six months of 1998. See Appendix A.

<sup>76</sup> *Universal Service Order*, 12 FCC Rcd at 9057; 47 C.F.R. §§ 54.507(c), 54.623.

<sup>77</sup> See *Universal Service Order*, 12 FCC Rcd at 9050. See also 47 C.F.R. § 54.505(c). The discount matrix is reproduced at Appendix D.

<sup>78</sup> *Universal Service Order*, 12 FCC Rcd at 9059-60; 47 C.F.R. § 54.507(g).

the most economically disadvantaged schools and libraries in accordance with the procedures set forth in section 54.709(g) of our rules.<sup>79</sup>

32. On September 10, 1997, the Common Carrier Bureau sought comment on several issues with respect to the application process and the distribution of universal service support for schools, libraries, and health care providers.<sup>80</sup> Among other things, the Bureau sought comment on whether the Commission should establish a filing window period, and what methods would "ensure a broad and fair distribution of funds, particularly at the earliest stages of these support programs."<sup>81</sup> The Bureau also sought comment on "whether a mechanism to prioritize requests from rural health care providers should be adopted in the event that requests exceed available funds."<sup>82</sup> In the *Third Report and Order*, the Commission adopted an initial filing window in order to give equal funding priority to all schools, libraries, and health care providers that apply for support at any time during the filing window, replacing the first-come, first-served approach for the first application filing period.<sup>83</sup> The Commission adopted the filing window to provide more time for schools, libraries, and health care providers to complete the necessary forms and to negotiate contracts in accordance with our competitive bidding requirement, as well as to reduce disparities among applicants with varied administrative resources.<sup>84</sup>

33. In addition to commenting on the adoption of a filing window, parties presented a wide range of suggestions for altering the rules of priority to ensure a broad and fair distribution of funds in response to the *September 10 Public Notice*.<sup>85</sup> In the *Third Report*

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<sup>79</sup> 47 C.F.R. § 54.507(g). Pursuant to section 54.507(g), when only \$250 million remains to be allocated, the SLC will notify the public and, during a 30-day period or the remainder of the funding year, whichever is shorter, will commit funds only to the schools and libraries in the two most economically disadvantaged categories. During the period, SLC will grant priority to the most economically disadvantaged schools and libraries that have not yet received universal service discounts. If funds remain after the 30-day period, the funds once again will be allocated according to the Commission's rules. *See id.*

<sup>80</sup> Common Carrier Bureau Seeks Comment on Universal Service Support Distribution Options for Schools, Libraries, and Health Care providers, CC Docket 96-45, *Public Notice*, DA 97-1957 (1997) (*September 10 Public Notice*). This Public Notice was published in the Federal Register on September 15, 1997. 62 Fed. Reg. 48280 (Sept. 15, 1997). Comments were filed on September 25, 1997.

<sup>81</sup> *September 10 Public Notice* at 2.

<sup>82</sup> *September 10 Public Notice* at 2.

<sup>83</sup> *Third Report and Order*, 12 FCC Rcd at 22486. In addition, the Commission concluded that SLC and RHCC may implement such additional filing periods as they deem necessary. 47 C.F.R. §§ 54.507, 54.623.

<sup>84</sup> *Third Report and Order*, 12 FCC Rcd at 22486.

<sup>85</sup> These commenters are listed in Appendix C.

and Order, the Commission clarified that, in the event that the \$250 million trigger was reached during the filing window, SLC, consistent with its function as Administrator, would be responsible for allocating funds in accordance with the Commission's rules of priority.<sup>86</sup> The Commission did not make any modifications to its rules of priority at that time. In the *Collection Public Notice*, the Common Carrier Bureau sought additional comment on ways to ensure that the most economically disadvantaged schools and libraries receive adequate universal service support.<sup>87</sup>

## B. DISCUSSION

34. *Schools and Libraries Support Mechanism.* Upon further consideration, we find that we must adopt additional new rules of priority to ensure that, when a filing window period is in effect, support is directed toward the most economically disadvantaged schools and libraries, as well as toward those located in rural areas. Consistent with the statute and the recommendations of the Joint Board, we have consistently focused on ensuring that the services eligible for universal service support are affordable for all eligible schools and libraries. Under the discount matrix, the most economically disadvantaged schools and libraries are eligible for the greatest levels of discount. For example, schools with between 75 and 100 percent of their students eligible for the national school lunch program are eligible for 90 percent discounts on all eligible services.<sup>88</sup> In the *Universal Service Order*, we established a priority system under which the most economically disadvantaged schools and libraries, those with over 50 percent of their student populations eligible for the national school lunch program, would have priority when only \$250 million available to be committed in a given funding year.<sup>89</sup> The rules of priority adopted in the *Universal Service Order*, however, were premised on the assumption that support would be distributed on a first come, first served basis. That is, the \$250 million trigger was established before the Commission adopted a window filing period. We conclude that we must adopt additional new rules of

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<sup>86</sup> *Third Report and Order*, 12 FCC Rcd at 22487-88.

<sup>87</sup> We note that several parties commented in response to the *Collection Public Notice* on certain administrative and access charge reform issues. Because these issues have no substantive bearing on the issues addressed in this Order, we do not respond substantively to those comments. See, e.g., AirTouch comments at 3 (end-user surcharges); GTE comments at 8 (same); Sprint comments at 3 (same); SBC comments at 2-4 (fundamental changes to schools and libraries universal service support mechanism); API comments at 3-4 (access charge reform and the productivity factor); RUPRI comments at 5 (high cost fund); USTA comments at 5 (high cost fund, SLC administrative expenses, support for telecommunications carriers only); Nassau BOCES comments at 2-3 (retroactive payments); NTIA comments at 2 (truth-in-billing, local plans for Internet use); CTIA comments at 1-4 (calculation of universal service contributions for wireless providers); ICA comments at 2 (access charge reform).

<sup>88</sup> See *Universal Service Order*, 12 FCC Rcd at 9050.

<sup>89</sup> *Universal Service Order*, 12 FCC Rcd at 9059-60.

priority premised on the existence of a filing window period during which all applications received within the window are treated as if filed simultaneously. We also conclude that new rules of priority are necessary to account for the fact that the support requested by schools and libraries during the initial filing window exceeds the total authorized support available for the funding period January 1, 1998 through June 30, 1999. Moreover, there is the possibility that support requested by schools and libraries during subsequent filing windows may exceed the total authorized support available in subsequent funding years. Therefore, we adopt new rules of priority that will operate when a filing window is in effect. We do not, however, alter the rules of priority for applicants that request support when a filing window is not in effect.<sup>90</sup> Although, in this initial 18-month funding period, only the applications filed during the initial 75-day filing window will receive support, it is possible that in future funding years support could be provided for applications filed outside of a filing window period.

35. The additional new rules of priority described below will equitably provide the greatest assurance of support to the schools and libraries with the greatest levels of economic disadvantage while ensuring that all applicants filing during a window receive at least some support in the event that the amounts requested for support submitted during the filing window exceed the total support available in a funding year. Because these rules of priority utilize the discount matrix, which provides higher discounts for schools and libraries in rural areas, they also equitably provide greater support to schools and libraries in rural areas. These rules, therefore, further implement the Commission's prior decisions to allocate support for schools and libraries in a manner that provides higher levels of support for rural areas and areas with greater economic disadvantage, while recognizing that every eligible school and library should receive some assistance.<sup>91</sup> Further, these rules of priority are consistent with the suggestions of several commenters.<sup>92</sup> Upon further consideration, we conclude that these

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<sup>90</sup> These rules are preserved in section 54.507(g)(2), as amended in this Order. See Appendix A.

<sup>91</sup> See, e.g., *Third Report and Order*, 12 FCC Rcd at 22486, 22487-88; *Universal Service Order*, 12 FCC Rcd at 9057-60.

<sup>92</sup> See Great City Schools comments at 4 (proposing priority rules that would permit full funding for schools and libraries eligible for 80 percent and 90 percent discounts and a proportional scale back of discounts for all other eligible schools and libraries). See also Anchorage School Dist. Sept. 10 Public Notice comments at 1 (stating that, if sufficient funds are not available to meet all approved applications in subsequent filing periods, the Commission should apply an equal percentage reduction to all approved applicants during period); Mississippi Council for Ed. Tech. Sept. 10 Public Notice comments at 4 (asserting that funds should be available first to the most disadvantaged schools and libraries); Montana School Boards Ass'n Sept. 10 Public Notice comments at 3 (supporting a mechanism similar to the rules of priority should be applied to all funds, not just \$250 million); New York City Dept. of IT&T Sept. 10 Public Notice comments at 3 (stating that, if funds are exhausted within the window filing period, distribution of funds should be subject to a pro-rata reduction based on economic disadvantage, obviating need of a \$250 million trigger); New York Pub. Library Sept. 10 Public Notice comments at 1 (advocating a filing window and pro-rata allocation of funds when only \$500 million remains for the year). But see RUPRI comments at 3-4 (stating that sole reliance on poverty and urban/rural

new rules of priority will best promote the universal service goals of the Communications Act.<sup>93</sup> Accordingly, we amend section 54.507(g) of our rules as indicated in Appendix A.

36. The additional new rules of priority for the schools and libraries universal service support mechanism shall operate as described herein for applicants that submit a request for support within an established filing window.<sup>94</sup> When the filing window closes, SLC shall calculate the total demand for support submitted by applicants during the filing window. If total demand exceeds the total support available in that funding year, SLC shall take the following steps. SLC shall first calculate the demand for telecommunications services and Internet access for all discount categories. These services shall receive first priority for the available funding. SLC shall then calculate the amount of available funding remaining after providing support for all requests for telecommunications services and Internet access. SLC shall allocate the remaining funds to the requests for support for internal connections,<sup>95</sup> beginning with the most economically disadvantaged schools and libraries, as determined by the schools and libraries discount matrix.<sup>96</sup> That is, schools and libraries eligible for a 90 percent discount shall receive first priority for the remaining funds, and those funds will be applied to their requests for internal connections. To the extent that funds remain, SLC shall next allocate funds toward the requests for internal connections submitted by schools and libraries eligible for an 80 percent discount, then for a 70 percent discount, and shall continue committing funds for internal connections in the same manner to the applicants at each descending discount level until there are no funds remaining.

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status is not the proper approach, but emphasis should be on total relative price after discount); Colorado Dept. of Ed. Sept. 10 Public Notice comments at 2 (opposing any proposal that limits the funds available to schools and libraries in the first six months because the Commission has chosen to collect only \$1 billion in the first six months); DataCast Sept. 10 Public Notice comments at 2 (favoring rules of priority that allocate 1/4 of all funds to rural, high cost schools and take into account "relative economic advantage" in allocating support); Illinois State Board of Dirs. Sept. 10 Public Notice comments at 10-12 (favoring granting states greater authority in implementing rules of priority, granting priority to schools with the least amount of infrastructure, and implementing a higher trigger level because current 10 percent trigger represents insufficient funds); Maine Dept. of Ed. Sept. 10 Public Notice comments at 2 (favoring allocation of support according to the Technology Literacy Challenge Grants formula).

<sup>93</sup> 47 U.S.C. §§ 151 *et seq.*

<sup>94</sup> We note this request will be submitted using FCC Form 471.

<sup>95</sup> In his dissent, Commissioner Furchtgott-Roth argues that we lack authority under section 254(h)(2) of the Act to provide discounts for internal connections. Statement of Commissioner Harold Furchtgott-Roth, dated June 22, 1998, at 9-11. As we have discussed at length in our prior orders, analysis of section 254(h)(2), in conjunction with other provisions of the Act, clearly demonstrates that such discounts are authorized. *See, e.g., Universal Service Order*, 12 FCC Rcd at 9084-90. *See also* Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report to Congress*, FCC 98-67, at 89, para. 185 (rel. April 10, 1998) (*April 10th Report*).

<sup>96</sup> See Appendix D, which reproduces the discount matrix adopted in section 54.505(c) of our rules.



37. If the remaining funds are not sufficient to support all of the funding requests that comply with the Commission's rules and eligibility requirements within a particular discount level, SLC shall divide the total amount of remaining support available by the amount of support requested within the particular discount level to produce a pro-rata factor.<sup>97</sup> Thus, for example, if all applicants eligible for discounts of 90 percent may be fully funded, but there are not sufficient funds remaining to fully fund internal connections for applicants eligible for discounts of 80 percent, SLC shall reduce the support level for each applicant that is eligible for an 80 percent discount by multiplying the appropriate requested amount of support by the pro-rata factor. SLC shall then allocate funds to each applicant within the 80 percent discount category based on this reduced discount level. SLC shall commit support to all applicants consistent with the calculations described herein. We expect that, for the initial 18-month funding period, the collection levels established in this Order will enable all of the applicants eligible for discounts of 90 percent to receive full support for internal connections, and that at least a substantial portion, if not all, of the support requested for internal connections by applicants eligible for discounts of 80 percent will be provided.

38. In light of our decision to reduce the collection levels for schools and libraries at this time, we find that our revised method of prioritization is the best way to provide substantial and predictable support for schools and libraries.<sup>98</sup> We conclude that, to the extent that we are unable at this time to fund demand fully, the best approach is to provide full support for recurring services, and to direct support for internal connections to the neediest schools and libraries. We agree with commenters who state that it would be the most economically disadvantaged schools and libraries that would suffer the most if internal

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<sup>97</sup> The pro-rata factor is calculated based on the amount of support requested that complies with the Commission's rules and eligibility requirements.

<sup>98</sup> See, e.g., U.S. Department of Education comments at 1 (stating that schools and libraries require predictability of funding to facilitate long-range technology planning); DTG comments at 4-5 (stating that "[t]he proposed revision of support collections after the initial round of applications is final imposes new risk and unpredictability on the process at a time when it should become more predictable if the goal of access to advanced telecommunications for all schools is to be met"); NC DPI comments at 3 (changing the rules at this point causes mistrust and economic hardship); Funds for Learning comments at 2 (asserting that schools and libraries need predictability, not more frustration, and that service providers may become disenchanted with the changing rules and potential loss of business has schools and libraries have to delay projects for which they anticipated receiving support).